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NortonLifeLock, Inc. (NLOK)

Q1 2023 Earnings Call

CORPORATE PARTICIPANTS

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Natalie M. Derse
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MANAGEMENT DISCUSSION SECTION

Mary Lai
Vice President-Investor Relations

GAAP AND NON-GAAP FINANCIAL MEASURES

- I'd like to remind everyone that during this call, all references to the financial metrics are non-GAAP and all growth rates are y-over-y, unless otherwise stated
- A reconciliation of non-GAAP to GAAP measures is included in our press release, which is available on our IR website at investor.nortonlifelock.com

Vincent Pilette
Chief Executive Officer & Director

Q1 HIGHLIGHTS

Acquisition of Avast, Digital Life Protection and Empowerment

- After a very lengthy process in the UK, we are pleased to have received provisional approval from the Competition and Markets Authority for the acquisition of Avast
- Our hard work has paid off and we are excited to start the process of bringing the two companies together, with a great purpose and mission of bringing digital life protection and empowerment to everyone
- As I have shared before, our two companies share a similar vision and both have common values and complementary strengths

- As soon as we can bring us together, we will get started on delivering all the benefits of our new company to consumers, shareholders and other stakeholders

PREMIUM PRODUCTS AND REVENUES

- Together, we will serve about 500mm users globally, sell premium products to consumers for more than $3.5B in revenue, and have around 4,000 employees dedicated to the mission of protecting and empowering people to live their digital life safely

Complementary Product Portfolio and Culture of Innovation

- Avast's strength in privacy and NortonLifeLock's strength in identity, supported by our combined AI capabilities, creates a broad and complementary product portfolio beyond core security and towards adjacent trust-based solutions
- On top of that, the merger will broaden our geographic diversification, increase our presence in multiple channels, and also serve very small businesses
- We will have the opportunity to empower millions of consumers around the world with our complementary product portfolio and culture of innovation
- And while the world is in a different place than when we started this journey over a year ago, one thing is for sure, people want to continue to enjoy the advantages of a digital world without compromising their security, privacy and identity
- And our sole mission is to bring that and more to everyone

FCF, Revenues and Gross Cost Synergies

- Our combined financial profile is substantially enhanced through increased scale, long-term growth potential, synergies, strong FCF generation, supported by a resilient balance sheet
- As I mentioned, based on our last reported financials for both companies, we will scale our combined revenue to over $3.5B.
- And the combinations will unlock significant value creation to approximately $280mm of annual gross cost synergies and will give us the capacity to reinvest for innovation, partnerships and marketing to further accelerate our transformation

Operating Leverage and EPS

- We will have created operating leverage of approximately 52% in blended operating margin, that is pre-synergies, delivering approximately $1.5B of annual FCF, also pre-synergies
- The combination is another value creation enabler as we march towards our long-term objective of $3 in EPS.

Integration Planning Activities

- We look forward to re-engaging with Avast and restarting the integration planning activities
- Once the transaction is closed, we will be able to share more details on the combined business and its financial model
- So in terms of what's next, we will continue to work closely as quickly as possible after the CMA publishes its final approval, which is currently expected to be in early September, subject to change
  - Based on what we know today, we anticipate the closing date of the merger is expected to be between mid-September and sometimes in early October

Bookings Growth and Currency

- So, with that, let me say a few words on our Q1 results
- While we observed the weaker consumer sentiment and inflationary pressure impacting the consumer discretionary spend, we are proud to deliver our 12th consecutive quarter of bookings growth, with Q1 bookings up 5% in constant currency and revenue up 6%
- The quarter's performance tracked in line with our mid-single digit bookings growth projection for FY2023, which I view as a demonstration of the stability that our business operating leverage provide in a challenging environment

Direct Revenues and Customer Count

- Our direct revenue grew 5% in constant currency on top of another strong COVID-led double-digit growth quarter a year ago
- In this new environment, our focus has been on balanced performance across a set of very healthy customer metrics
- Total customer count was stable at over 23.3mm, up 200,000 y-over-y, but down 200,000 sequentially
    - Throughout the quarter, we saw the impact of the macro-level headwinds in our direct-to-consumer website global traffic, slightly offset by solid conversion rates
- While these headwinds have limited our ability to grow customer count this quarter at the pace we aspire to, it's important to highlight that our overall customer base is healthy, with stable retention rates, stable ARPU and opportunity to continue to drive cross-sell, upsell, as we launch new products

Retention Rate and consumer Cyber Safety

- Our retention rate remained very strong at slightly over 85% in unit
- Customer cohorts who joined during the so-called COVID period have retention rates at par with prior years and through our operation initiatives, we continue to make progress in first-year renewal rates
- Our efforts have led to happier customers, supported by-products that are easier to download and easier to use
    - Since we became a dedicated consumer Cyber Safety company, we have grown our direct customer base by proximately 3mm to reach over 23mm customers and at the same time, improved our retention rate by almost 1 point during the period

Partner Business

REVENUES AND BOOKINGS GROWTH

- Another set of activities we are focused on is delivering more value to more customers in our partner business
- In this set of indirect channels, we delivered double-digit revenue growth for the seventh straight quarter, up 16% in constant currency, in this Q1 FY2023
- We had very healthy bookings in Q1, including double-digit bookings growth in both mobile and employee benefit channels, channels in which we added approximately 200,000 customers y-over-y and stayed flat sequentially
- As we continue to build a more global and more diversified go-to-market model, we look forward to combining with Avast, which will allow us to accelerate our strategy of expanding identity and privacy solutions across the globe

PRODUCT PORTFOLIO

- A year ago, we stated that we would transform our company by building a richer product portfolio and we have continued to work towards that
  - We are off to a good start in FY Q1 on the product side

Norton Identity Advisor Plus

- In Q1, we have made good inroads from our recent launch of the Norton Identity Advisor Plus for the UK market and we've expanded the product's availability to Australia, New Zealand and Germany
  - This is yet another example of our international expansion efforts bolstering our identity capabilities

NORTON 360 WITH LIFELOCK PRODUCT, ASSESS AND PRIORITIZE

- We also continue to earn positive product reviews from important technology reviewers
- Just last month, we were awarded PC Magazine number one identity theft protection software for 2022
- Specifically, this was Norton 360 with LifeLock product, awarded to provide the best overall identity protection in the industry
  - This is just one of the many times we have been recognized for our overall product innovation and development efforts
- We continuously assess and prioritize our product roadmap and we know we still have big opportunity to expand our product portfolio, especially in areas beyond core security
- But above all, what guides us is our focus on providing quality and value in our products
- It is about a seamless end-to-end customer experience and comprehensive protection while making it simple for consumers to engage with us and stay safe

Cyber Safety

- Cyber safety will continue to be an evolving and growing market, fueled by the increase in activities online which brings more risk and challenges to consumers' digital lives
- With the merger with Avast, together we are well-positioned to drive the transformation of Consumer Cyber Safety and pursue our long-term objective while being financially resilient in any environment that comes ahead of us

Natalie M. Derse
Chief Financial Officer

FINANCIAL HIGHLIGHTS

GAAP and Non-GAAP Financial Measures

- For today's discussion, I will start with Avast updates followed by our Q1 performance details and our outlook for Q2 FY2023
- I will focus on non-GAAP financials and y-over-y growth rates unless otherwise stated

Merger with Avast and Pre-Integration Blending

- I'd like to echo Vincent's excitement about the merger with Avast

- We are thrilled to have this positive outcome and look forward to closing the acquisition
- We will immediately restart our pre-integration blending efforts as we prepare to scale the combined company and work to achieve the $280mm of annual gross cost synergies

Financing Package, Interest Rate Environment and EPS

- Let me give you a quick refresher on the transaction financing done in conjunction with the merger, which we successfully raised earlier this year
- In total, our financing package is comprised of $7.6B of term loan A and term loan B that spreads a 1.5% to 2% plus $1.5B revolving credit facility
    - This will replace our existing $1.7B term loan A facility and $1B revolver
- While the interest rate environment has changed since we first announced the merger last year, we still feel good about the rates we were able to lock in
- The acquisition financing will become funded as the deal closed
    - Once the deal is closed, we will share more information on our long-term model and the timing of our $3 EPS objective

FX Environment

- Now, on to our Q1 results
- Q1 was a good start to our FY2023, especially considering the macroeconomic pressures and volatile FX environment
- Our business is resilient, our customer base is healthy, and we continue to execute with discipline

Revenues and Currency

- Our Q1 revenue was $708mm, up 6% in constant currency and up 2% in USD including a four-point currency headwind translating to a revenue headwind of $27mm y-over-y
- Similar to last quarter, we saw continued currency volatility with both the euro and yen depreciating further against the US dollar reaching 20 year lows
- It is the third straight quarter in which currency has been several points of headwind to our top line on growth
- We anticipate these headwinds will remain for a full-year of compares as we plan the business at today's exchange rate with euro and USD near parity and a weaker yen
    - Despite these macro headwinds, we remain focused on execution against our business opportunities and driving towards our long-term objectives

Bookings and New Identity Solutions

- Q1 bookings grew 5% in constant currency on top of a 10% constant currency bookings growth in Q1 last year and in line with our full-year projection of mid-single digit rate of growth
- We've launched new identity solutions, and we've seen an increase in both geographic reach and adoption

Identity and Privacy Products

- Our expansion efforts are working as Q1 was our sixth straight quarter of high-single digit rate of growth in our identity and privacy products
- Our direct revenue grew 5% in constant currency and 1% in USD, impacted by 4 points of FX headwinds

Operating Metrics and ARPU

- Looking across our other key operating metrics, Q1 direct customer account grew by approximately 200,000 y-over-y, but declined by approximately 200,000 q-over-q as we saw headwinds in select markets
- Overall, customer unit retention remains stable above 85%, and we continue to drive incremental improvements to key cohorts, including our newer customers
- Our monthly average revenue per user, or ARPU, was $8.82
- However, adjusted for FX, ARPU expanded nearly $0.30 y-over-y and expanded $0.07 sequentially, an indication of our successful cross-sell efforts
    - We have a very healthy, resilient customer base and we remain focused on driving new customer acquisitions, retaining our existing customers, as well as increasing engagements with new products and services

Partner Business

- Turning to our partner business
- Partner revenue was up 16% y-over-y in constant currency, up 10% in USD and marks the seventh consecutive quarter of double-digit growth
- We see traction with our identity expansion efforts through partners, driving strong growth in our employee benefits channel and scaling key international partnerships like TELUS.
- Diversification and expansion of our go-to-market channels is the key growth tenet in our long-term plan, and we will continue to invest in these areas

Profitability

- Turning to profitability
- In Q1, we achieved gross margin of 86%, roughly flat year-on-year, while at the same time expanding and adding more features to our product offerings
- Our operating margin for the quarter was 54%, up 250BPS y-over-y, driven by both our revenue growth and our cost discipline, with overall spend down 3% y-over-y
- As you've heard me say before, we are intentional with our investments and how we fund our business to drive future growth
- Our G&A functions remain lean, with spend at less than 4% of revenues for Q2 in a row

R&D and Cost Structure

- With regards to R&D, we continue to be disciplined and invest in new product development and innovation
- With our marketing dollars, we strive to balance across the portfolio and across channels with intentional customer acquisition targeting, while focusing on long-term sustainable growth
- We will continue to be disciplined with our cost structure across all functional areas as we operate in this increasingly challenging environment

Net Income and EPS

- Q1 net income was $265mm, up 7% compared to last year

- Diluted EPS was $0.45 for the quarter, up 7% y-over-y, including $0.03 of currency headwind and above the high end of our guidance range
- Adjusting for the impact of currency, EPS grew more than twice the rate of revenue at 14% y-over-y
  - We remain committed to driving EPS expansion and achieving our long-term EPS objective of $3

CASH FLOW AND BALANCE SHEET ITEMS

- Turning to our cash flow and balance sheet
- Q1 operating cash flow was $215mm, and FCF was $213mm
- In Q1, we returned nearly $400mm back to shareholders
- We repurchased $300mm or 12mm shares in buybacks in the quarter, and now have approximately $1.5B remaining in the current share buyback program

Dividend

- We paid approximately $73mm to shareholders in the form of a regular quarterly dividend of $0.125 per common share
- For Q2, the board of directors has approved a regular quarterly cash dividend of $0.125 per common share to be paid on September 14, 2022 for all shareholders of record as of the close of business on August 22, 2022, as described in the press release

Net Debt Leverage and Cash

- Separate from the transaction financing I discussed earlier, our net debt leverage was approximately 1.4 times in the quarter
- We settled in cash our $400mm senior unsecured notes that matured in June
- We also plan to settle in cash our 2% senior convertible note due in the middle of August, and that cash settlement will hit our cash flow in fiscal Q2
- As we all know, the debt environment has been volatile and rapidly changing
- We will continue to assess our overall debt needs and leverage profile
- Given our high cash flow generation and strong levels of liquidity, we are confident in our ability to manage through this environment accordingly

OUTLOOK

Currency

- Now, turning to our Q2 outlook
- Based on the continued strengthening of the US dollar quarter to date, we anticipate an even larger currency headwind
- But I want to emphasize that the underlying health of our business remains strong

Revenues and EPS

- For Q2, we expect non-GAAP revenue in the range of $695mm to $705mm, which translates to mid-single-digit rate of growth y-over-y in constant currency and reflects a projected FX headwind of 4 plus points of growth, or approximately $30mm

- We expect Q2 non-GAAP EPS to be in the range of $0.44 to $0.46 per share, which reflects $0.03 of currency headwind y-over-y
- Our Q2 guidance assumes the Avast deal closes in early October 2022

FY2023

BOOKINGS, AVAST MERGER AND PLAN

- For FY2023, we continue to expect bookings growth to be in similar ranges of mid-single digits in constant currency
- Considering the close timing of the Avast merger, we will not be providing an annual guidance at this time
- We plan to provide more details on our overall financial model when we close the transaction

QUESTION AND ANSWER SECTION

Saket Kalia
Barclays Capital, Inc.

Q

Maybe before we talk about Avast, I was wondering if you could touch on some of the dynamics between your partner business and the direct business. It just feels like there's been a little bit of a shift between those two routes to market. And so maybe the question is, is that intentional? And can you just walk us through what's happening there especially given the decline, the sequential decline in direct subs this quarter?

Vincent Pilette
Chief Executive Officer & Director

A

So, definitely, as you know, we have been investing in our partner channels. We have been saying that now for many, many quarters, it represents about slightly above 10% of our overall business. And we believe that there is more opportunities to go through other channels in order to partner with other solution providers to provide a combined solution to consumers. I mentioned the two channels we like. Of course, it's the mobile channel. Some of our competitors have moved that channel into direct. It basically goes through app stores and it's not in our direct business today because of the billing definition, it doesn't go to us directly. But to be honest with you, the consumers gets on our platform and we have direct access to them and communicate and provide value. So that has been growing. We're seeing definitely a shift towards mobile users. A few quarters ago, we crossed the Norton 360 platform to be the majority of the products sold on the mobile, which is a very good sign. And you will see us continue to move up in that channel with momentum.

The second one is employee benefits. It goes through employers that offer to their employees' full protection in the cyber world, identity protection, privacy and device security. There are two. We have the direct engagement with the customers on our LifeLock platform, but the payment goes through the payroll of the company that supports that. We believe we have more to go in mid-market. We probably need to invest in our direct sales, partnering with a broker to penetrate that. And you'll see continued growth and focus both on the product marketing, development side as well as the channel side. So those are the direct engaged customers in our partner business.

Then we have another set of channels that go and combine with other providers of other solutions to provide a full package. So here like, for example, the partnership with TELUS in Canada to bring cyber safety along with the TELUS solutions to Canadians had a very strong momentum. And you will see us continue to expand.

Travis Witteveen, who was the CEO of Avira, has ton of experience in the environment has become our customer acquisition chief if you want a few quarters ago. And he's developing his team, and along with his team, they are definitely building up the funnel of new opportunities. So you'll see us continue to invest in that.

I do want to say a few words on the direct business. The direct business you mentioned, the sequential slight decline and you are right on that. The metrics are very healthy. Retention rates have been very strong across all cohorts. We said a year ago we would improve the first-year retention rate and we have by a few points. Over the last 24 months, we have increased overall retention by a little more than 70BPS. And so, you'd see continued operational initiatives, whether it's on how the product is being downloaded, how it's being used, how the value is demonstrated to the customers that improve customer satisfaction and then overall retention. So, strong focus on that healthy set of customers.

The gap or disappointment if you want for the quarter is really related to the macro level headwinds that we saw with lower traffic of global traffic on that cyber safety website if you want. Conversion rates still holding well but it's about traffic. It was volatile. There were pockets of weaknesses, other pockets of areas where we continue to invest because we are here for the long term. And as we navigate through a volatile environment, we know we provide a product that will be needed in an area that has structural growth.

Saket Kalia
Barclays Capital, Inc. Q

The operating margin here continues to really outperform and be higher than expected. Can you just talk about how you're balancing investing in new customer acquisition vs. managing for profitability? How do you think about that?

Natalie M. Derse
Chief Financial Officer A

Operating margin of 54% now for two quarters and up 250BPS y-over-y, we're proud of that. That points toward a healthy business model we have and combined with our team's commitment to operate in a disciplined manner. New acquisition is absolutely a key tenant of our overall growth strategy. We've been clear about that. But it's not the only one. We have multiple levers to help drive our growth, and it's not growth at all costs. And that's where the balance comes in.

We've continued to invest in customer acquisition marketing. You can see that. We talk about we spent a lot of time focused on that, both through our direct channels and now as well even more so in our partner channels. We're committed to the growth focus approach when it comes to sales and marketing. And honestly we recognized what a competitive industry we operate in and that consumers have choice, and we need to work really, really hard to win that choice.

But in addition to investing in marketing where we've been investing more and more is in product. We've launched some really cool, several new offerings. We continue to diversify the go-to-market channels. We continue to invest in our customer service offering. And I think from that combination of investment, that's where that ARPU growth is really coming from, both y-over-y and q-over-q, and it allows us to sustain and scale our unit retention of 85% plus, both proof points of the healthy acquisition that we've seen over the last ten quarters. That combined with we stay committed to operating G&A as lean as possible, the last two quarters being less than 4% of our revenue, obviously provides us a lot of leverage for reinvestment.

So, as we navigate forward, we'll continue to balance the growth and profit. Both are important. I don't think we have to pick. I'm confident we will find a way to strike that right balance through the disciplined approach that we've applied for now since we've stood up NortonLifeLock. And above and beyond all that, we're just very, very excited about the additional opportunities we have as we combine with Avast.

Saket Kalia
Barclays Capital, Inc.

Q

If I can squeeze a third one in, Vincent, maybe for you. We can't go on without asking a question on Avast. And I know that we can't talk too much about specifics until the deal is closed. But maybe philosophically, as you've gotten to know Avast's business more and studied this market more, I guess how do you think about potential revenue synergies with the combination of NLock and Avast? I mean, certainly, you were clear about the expense side. Just as you spend more and more time with really both companies, how do you think about the revenue synergies between the two?

Vincent Pilette
Chief Executive Officer & Director

A

I would be very disappointed not to have a question on Avast. I think this is a very, very exciting news. Talked to Ondrej yesterday. I know the Avast team is also super excited about coming together, and we know we are about to create the foundation of an even stronger company with a very broad mission of that digital freedom for digital life.

We discussed that a few quarters ago, but when we made the acquisition model or the transaction model, we based the merits of this transaction on cost synergies, overlapping activities, to the tune of $280mm that I've talked about. And we wanted to have the value of that transaction to be based on that. We also said we would reinvest a portion to accelerate the top line growth or transform the profile of our revenue.

We did not include in our acquisition model revenue synergies for many reasons, but certainly not the reason that it will be our priority number one as soon as we close. We see the opportunity. And I see three buckets of opportunity, if you want, conceptually, without giving any numbers.

The first one is on the retention side. NortonLifeLock has developed a set of capabilities and operations and experience that drive high NPS and retain at 85% in unit. That equivalence number is 68% in Avast, at least in the last reported numbers. And we know that we can bring a lot of the practices and the approaches as we bring a stronger portfolio to the consumers to improve that retention rate. There may be some mix differences by geography or product mix. But even when we compare during due diligence, our number, we know we have opportunities there. So that's bucket number one.

The second one is the cross-sell/upsell capabilities. We've just introduced those capabilities in NortonLifeLock about a year-and-a-half ago. And we know Avast has been developing their entire business model on that, offering a basic product for free, and then delivering, showing, demonstrating more value to the consumers to a point where the consumer is ready to pay for that value. And then, growing that value offered to the consumers.

We look forward for Avast to bring those operational skill sets, if you want, into our overall combined company while we bolster a richer portfolio. So identity, a LifeLock equivalent services that we started to expand internationally, will be offered to Avast customers, as an example. And Avast has had to focus more on privacy. When you combine the two, it will be a very rich portfolio to cross-sell and deliver more value to consumers. That's the second set of revenue synergies.

And then, the third one is across the complementarity of the geographical footprint, whether it's US vs. international from our standpoint, from their standpoint, Europe vs. the rest of the world. But even then, they were more about emerging markets; we're more about Western market. And so, I see a lot of complementarity. As we bring a richer company together, locally, we can accelerate our penetration, including in the VSB or very small and small business area, where Avast has already a small channel and where, as you know, we are not present. Yet, some of those businesses have exactly the behavior of consumer.

So the third bucket is around geographical footprint and expanding the channel as we come together. As soon as we close the acquisition, I can tell you, we'll be – the first task we'll get started on that. And then, as soon as we are ready and the deal is closed, we'll share more with investors what our long-term plan is in this area.

Simran Biswal
RBC Capital Markets LLC

Q

So we were just looking and thinking about the current macros and how security seems to be more resilient. So we were wondering how you were thinking about the durability of these consumer security trends.

Vincent Pilette
Chief Executive Officer & Director

A

And when we talk about security, we really talk about, for us, Cyber Safety, which is not only your device security, but it's also the protection of your digital identities, all the way to the restoration and insurance you can have when something is breached from your device or from any transaction that can be processed into the cloud.

We know that cybercriminals continue to increase. I was reading a report earlier on that, it was like up 7% in H1 just in Europe. And so, we'll continue to see pressure from that. We know consumer penetration in term of full protection is not yet at the level of other protection industries, such as insurance industries or others. And so, we have more room.

We feel really good about the long-term structural growth opportunity that markets offer and that together with Avast, we will address and continue to expand. Now, it does not mean, of course, that in the short term, you still have volatility, you have inflationary pressures, you have consumer sentiment, and people will look at some of those costs and may see this as a discretionary spend. So, we definitely have pressure. We saw it in our global traffic this quarter.

But at the same time, we have a lot of levers to drive and deliver the value. 85% of the business is coming from the renewal base. And once the consumer is in, we've seen very stable retention rates through the last quarter, but frankly also, as I studied the business when I came in two years ago, it was similar behavior in 2008 or 2009. So, you see a lot of resilience into people who already know they need security on or in the digital world even though volatility may put pressure on new customer acquisition in the short term.

Simran Biswal
RBC Capital Markets LLC

Q

And just a quick follow-up from the customer perspective. You mentioned really healthy customer metrics and cross-sell has been accelerating and great execution on that front. So, how are you thinking about customer additions and upsell in a more challenging macro over these next few quarters?

Vincent Pilette
Chief Executive Officer & Director

A

Well, the good news once a customer is in and has a basic protection is that we can also make them aware of the moment of truth that we call Insight, which is a moment at which you connect to the internet when you're at the coffee shop or the moment you transfer data on the web and ensuring and monitor that you fully are protected, at which point in time, we can then raise the value to you of being fully protected vs. partially protected.

And so, constant assessment in finding the right moment give us the opportunity to continue to cross-sell. We still have the vast majority of our customer – customer base to be in the first part or the lower value part of our total value curve, if you want, from basic device security all the way to like full protection. So, we still have a lot of room to continue to educate and drive and demonstrate the value as the consumers move up the value chain.

Fiona G. Hynes
Morgan Stanley & Co. LLC

Q

It's sounding like from previous commentary on this call that, going forward, a big part of driving growth between Avast and NortonLifeLock is going to be the pairing of identity and privacy offerings. So, I was wondering if you could give us some more tangible use cases of how consumers can use those, like, basically, bundle those two different offerings together? And what's kind of your vision going forward for that cross-sell motion? Thank you.

Vincent Pilette
Chief Executive Officer & Director

A

So, we'll talk about cross-sell, upsell, revenue synergies when the deal is closed. But conceptually, it's all about completing the value of all of the use case you protect the consumer for and refining how you communicate in the app or on the platform all of the risk the consumer face is an important one. It's a fine balance, too. You want to do it respectfully and demonstrating the value at the same time. We know that the entire identity protection or theft protection, restorations and insurance is something Avast does not have and we can really offer as we combine that with security.

Avast started to move from security to privacy. They have BreachGuard, other views. And so, combining the product portfolio, working on the integrated platform, they have Avast One. We have Norton 360. We'll have to figure that out. And then, leaving product value that customer can step in once they have basic – as I mentioned, most of our customer in the basic platform have basic benefit to see how they move to the next one. The practices are about the same. At the end of the day as the product portfolio become richer, it's all about the ease of use, ease of downloading, how you use that. And we've made a lot of effort on our products to do that and expect us to continue as we come together.

Fiona G. Hynes
Morgan Stanley & Co. LLC

Q

Maybe one more follow-up if I could, another question touching on the macro.

Fiona G. Hynes
Morgan Stanley & Co. LLC

Q

Obviously, we see there are some headwinds in the customer acquisition this quarter. I was curious for your view and your sense of how much of that is just traditional seasonality given it's the summer months and PC shipments are seasonally weaker around this time period. And how much of that is kind of what you're seeing on the ground real-time in terms of potentially moderating macro environment? Thank you.

Vincent Pilette
Chief Executive Officer & Director

A

Definitely, we historically had Q3 quarters, which is fiscal Q3 for us, which is a December quarter, being stronger more on the security side and April quarter, our Q4 quarter, being strong on the identity side linked to some events such as tax and other things. To be honest with you, over the last two years, whether it's because of COVID or other macro level as well as the fact that we more and more provide one combined value of full total protection, we've seen less seasonality. But you're right that in the moderate seasonal effect, if you want, the June quarter would be a low quarter. So, from that perspective, our expectation was in line to a lower seasonality.

With that said, we did see some headwinds, what we call pocket of weaknesses, where we continue to invest at the same rate, because we know we're here for the long term and it's a portion of our investment that goes towards education. But we saw lower traffic. And so, we're really monitoring and flipping across the set of channels we have here to try to improve the return on our marketing spend.

Natalie M. Derse
Chief Financial Officer

A

I just think – when you think about – even as a consumer, you feel the macroeconomic environment, you feel inflation, you feel pricing pressures. I would combine that with some of the other markers that we see across the industry with PC shipments down now double-digit, not that we're entirely connected to that, but it's just another marker that shows us what's happening in our industry.

And it just – it honestly fuels us. We've got to be much, much more intentional. We've got to be much, much more competitive in order to win over the customer choice that's available. And then we do – through a disciplined approach, we spent so much time and effort making sure that those customers are as highly engaged as possible. We provide great customer service and we want to be fulfilling as much of that Cyber Safety need as we possibly can. So, that's where we spend most of our time.

Vincent Pilette
Chief Executive Officer & Director

CLOSING REMARKS

- I would like to take a moment to thank our NortonLifeLock team for contributing to our success each and every day
- As you've heard me say before, we truly have an ambitious team dedicated to the mission of the business we are building
- I would also like to say a few words on the upcoming change on our board of directors
- On behalf of the board and the leadership team, I want to thank Ken Hao for his contributions to the company over the last six years, helping NortonLifeLock through the successful transition to a standalone consumer Cyber Safety company and unlocking tremendous shareholder value
- Ken has been a great board member and also a trusted partner to me as a first-time CEO
- We wish him well and I'm sure we will stay in touch.
- We have been waiting for 12 months for the approval of our deal with Avast and we're so ready to dive in
    - I talked to Ondřej yesterday, as I mentioned, and I know that the Avast team feels exactly the same way
- The company is well positioned to deliver long-term value in pursuit of our vision
- So, thank you for joining and for your continued support of our company and our team

NORTONLIFELOCK PROFIT FORECAST

This document contains the following statement regarding NortonLifeLock's anticipated earnings per share ("**EPS**"):

"*We expect Q2 non-GAAP EPS to be in the range of $0.44 to $0.46 per share, which reflects $0.03 of currency headwind year-over-year.*"

The above statement (the "**NortonLifeLock Profit Forecast**") constitutes an ordinary course profit forecast for the purposes of Rule 28.1(a) and Note 2(b) on Rule 28.1 of the UK's City Code on Takeovers and Mergers (the "**Code**").

Notes

References to "GAAP" in the NortonLifeLock Profit Forecast are to U.S. GAAP, being the accounting policies applied in the preparation of NortonLifeLock's annual results for the year ended April 1, 2022. The press release published by NortonLifeLock on August 4, 2022, being the same date as the earnings call of which this document constitutes a transcript, contains the following explanation regarding non-GAAP financial measures:

"*We use non-GAAP measures of operating margin, net income and earnings per share, which are adjusted from results based on GAAP and exclude certain expenses, gains and losses. We also provide the non-GAAP metrics of revenues, constant currency revenues, and free cash flow, which is defined as cash flows from operating activities, less purchases of property and equipment. These non-GAAP financial measures are provided to enhance the user's understanding of our past financial performance and our prospects for the future. Our management team uses these non-GAAP financial measures in assessing NortonLifeLock's performance, as well as in planning and forecasting future periods. These non-GAAP financial measures are not computed according to GAAP and the methods we use to compute them may differ from the methods used by other companies. Non-GAAP financial measures are supplemental, should not be considered a substitute for financial information presented in accordance with GAAP and should be read only in conjunction with our consolidated financial statements prepared in accordance with GAAP. Readers are encouraged to review the reconciliation of our non-GAAP financial measures to the comparable GAAP results, which is attached to our quarterly earnings release, and which can be found, along with other financial information including the Earnings Presentation, on the investor relations page of our website at Investor.NortonLifeLock.com. No reconciliation of the forecasted range for non-GAAP EPS guidance is included in this release because most non-GAAP adjustments pertain to events that have not yet occurred. It would be unreasonably burdensome to forecast, therefore we are unable to provide an accurate estimate*."

Basis of preparation

The NortonLifeLock Profit Forecast has been prepared on a basis consistent with NortonLifeLock's accounting policies, as summarized in the paragraph entitled "Notes" above. The NortonLifeLock Profit Forecast excludes any transaction costs attributable to the merger (the "**Merger**") of NortonLifeLock and Avast plc ("**Avast**") or any other associated accounting impacts as a direct result of the Merger.

Assumptions

The NortonLifeLock Profit Forecast is based on the assumptions listed below.

Factors outside the influence or control of the NortonLifeLock Directors:

- There will be no material changes to existing prevailing macroeconomic or political conditions in the markets and regions in which NortonLifeLock operates.
- There will be no material changes to the conditions of the markets and regions in which NortonLifeLock operates or in relation to customer demand or the behavior of competitors in those markets and regions.
- The interest, inflation and tax rates in the markets and regions in which NortonLifeLock operates will remain materially unchanged from the prevailing rates.

- There will be no material adverse events that will have a significant impact on NortonLifeLock's financial performance.
- There will be no material adverse events that will have a significant impact on the timing and market acceptance of new product releases and upgrades by NortonLifeLock.
- There will be no business disruptions that materially affect NortonLifeLock or its key customers, including natural disasters, acts of terrorism, cyber-attack and/or technological issues or supply chain disruptions.
- There will be no material changes to foreign exchange rates that will have a significant impact on NortonLifeLock's revenue or cost base.
- There will be no material changes in legislation or regulatory requirements impacting on NortonLifeLock's operations or its accounting policies.
- There will be no new material litigation and no unfavorable resolutions of existing material litigation in relation to any of NortonLifeLock's operations.
- The announcement of the Merger will not have any material impact on NortonLifeLock's ability to negotiate new business.

Factors within the influence and control of the NortonLifeLock Directors:

- There will be no material change to the present executive management of NortonLifeLock.
- There will be no material change in the operational strategy of NortonLifeLock.
- There will be no material adverse change in NortonLifeLock's ability to maintain customer and partner relationships.
- There will be no material acquisitions or disposals.
- There will be no material strategic investments over and above those currently planned.
- There will be no material change in the dividend or capital policies of NortonLifeLock.
- There will be no unexpected technical or network issues with products or processes.

NortonLifeLock Directors' confirmation

With the consent of Avast, the Panel on Takeovers and Mergers has granted a dispensation from the Code requirement for NortonLifeLock's reporting accountants and financial advisers to prepare reports in respect of the NortonLifeLock Profit Forecast.

The NortonLifeLock Directors have considered the NortonLifeLock Profit Forecast and confirm that it has been properly compiled on the basis of the assumptions set out in this document and that the basis of the accounting used is consistent with NortonLifeLock's accounting policies.

QUANTIFIED FINANCIAL BENEFITS STATEMENT

This document contains statements of estimated cost savings and synergies arising from the Merger (together, the "**Quantified Financial Benefits Statement**"), which require certain disclosures under the Code.

A copy of the Quantified Financial Benefits Statement is set out below:

> "*Given the complementary nature of both NortonLifeLock and Avast, the NortonLifeLock Directors believe that the Merger will generate synergies that could not be achieved independently of the Merger and will lead to significant long-term value creation for all shareholders.*
>
> *Significant recurring cost synergies opportunity*
>
> *NortonLifeLock anticipates that the Merger will result in recurring annual pre-tax gross cost synergies for the Combined Company to reach a run-rate of approximately USD 280 million, representing between approximately 15% and 20% of combined adjusted cost of sales and operating spend, based on the latest full year reported results for each of NortonLifeLock and Avast. The synergies are expected to be fully realised by the end of the second year following completion of the Merger.*
>
> *NortonLifeLock intends to approach integration with the aim of retaining and motivating the best talent and structure across the Combined Company to create a best-in-class organisation. The expected sources of the identified cost synergies are as follows:*
>
> - *Organisation: approximately 50% of the total annual run-rate pre-tax gross cost synergies are expected to be generated through the adoption of shared best practice across existing functions and the reduction of duplicate roles across all geographies, and from a broad range of job categories, including management, shared services, product and commercial functions;*
> - *Systems & Infrastructure operating costs: approximately 25% of the total annual run-rate pre-tax gross cost synergies are expected to be realised through migration onto a common data and security platform, integration of systems, and shared technology and analytics infrastructure; and*
> - *Contracts & Shared Services: approximately 25% of the total annual run-rate pre-tax gross cost synergies are expected to be generated primarily from site rationalisation, procurement and vendor consolidation, and spend de-duplication.*
>
> *NortonLifeLock expects to realise approximately 60% of the run-rate cost savings by the end of the first full year following completion of the Merger and 100% by the end of the second full year following completion of the Merger, excluding any potential synergy reinvestment and associated benefits. On a reported basis, the synergies assume the Combined Company expects to benefit from approximately USD 75 million of cost savings in the first full year following completion of the Merger, approximately USD 245 million of cost savings in the second full year following completion of the Merger, and the full USD 280 million of the cost savings in the third full year following completion of the Merger, excluding any potential synergy reinvestment and associated benefits.*
>
> *One-off costs*
>
> *In order to realise these synergies, NortonLifeLock is expected to incur one-off restructuring and integration costs of approximately one year's run-rate pre-tax cost savings, or USD 280 million, with approximately USD 180 million estimated to be incurred in the first full year following completion of the Merger and approximately USD 100 million estimated to be incurred in the second full year following completion of the Merger. Aside from integration costs, no material dis-benefits are expected to arise in connection with the Merger. The expected synergies will accrue as a direct result of the Merger and would not be achieved on a standalone basis.*

The paragraphs above relating to expected cost synergies constitute a "Quantified Financial Benefits Statement" for the purposes of Rule 28 of the Code.

Given the strong strategic, cultural and operational fit of the two companies, NortonLifeLock believes that the quantified cost synergies are readily achievable.

NortonLifeLock expects to achieve the quantified cost synergies while maintaining appropriate investment levels in sales and technology to meet the Combined Company's growth targets and other objectives.

The estimated cost synergies referred to above reflect both the beneficial elements and the relevant costs."

Further information on the bases of belief supporting the Quantified Financial Benefits Statement, including the principal assumptions and sources of information, is set out below.

Bases of belief and principal assumptions

In preparing the Quantified Financial Benefits Statement, a synergy working group comprising senior strategy, operations, technical, sales and financial personnel from NortonLifeLock (the "**Working Group**") was established to identify, challenge and quantify the potential synergies available from the integration of the NortonLifeLock and Avast businesses, and to undertake an initial planning exercise.

In preparing the detailed synergy plan, both NortonLifeLock and Avast have shared certain operating and financial information to support the evaluation of the potential synergies available from the Merger and have conducted a series of virtual meetings with the key management personnel of both NortonLifeLock and Avast. This has included input from both the NortonLifeLock and Avast executive leadership teams.

Based on the information shared and interactions with Avast, the Working Group has performed a bottom-up analysis of costs included in the NortonLifeLock and Avast financial information and has sought to include in the synergy analysis those costs which the Working Group believe will be either optimized or reduced as a result of the Merger. In circumstances where the information provided by Avast has been limited for commercial or other reasons, the Working Group has made estimates and assumptions to aid its development of individual synergy initiatives. The assessment and quantification of the potential synergies have in turn been informed by NortonLifeLock management's industry experience as well as their experience of executing and integrating acquisitions in the past.

The baseline used as the basis for the Quantified Financial Benefits Statement is NortonLifeLock's adjusted cost base for the financial year ended 2 April 2021, supported where relevant by certain information from NortonLifeLock's budgeted cost base for the financial year ending 1 April 2022, and Avast's adjusted cost base for the financial year ended 31 December 2020, supported where relevant by certain information from Avast's budgeted cost base for the financial year ending 31 December 2021.

The quantified synergies are incremental to NortonLifeLock's and, to the best of NortonLifeLock's knowledge, Avast's existing plans.

In general, the synergy assumptions have in turn been risk adjusted, exercising a degree of prudence in the calculation of the estimated synergy benefit set out above.

In arriving at the estimate of synergies set out in the Quantified Financial Benefits Statement, the NortonLifeLock management has made the following assumptions:

- regarding organisational savings:
    - savings will be possible by removing duplicate resource through the roll-out of the revised operating model;

    - the enlarged group following the Merger (the "**Combined Company**") will be able to standardise and roll-out best practice systems and procedures, to generate efficiency and enable headcount reductions; and

    - no restrictions or delays will arise as a result of industrial relations or employment agreements that significantly affect the realisation of savings by removing duplicate resource;

- there will be no material impact on the underlying operations of either company or their ability to continue to conduct their businesses, including as a result of, or in connection with, the integration of the Avast group and the NortonLifeLock group;

- the Combined Company's product offering generates at least the same level of total revenues as the Avast group's and NortonLifeLock group's offerings currently generate;

- procurement savings can be realised through rationalising suppliers and renegotiating supplier terms;

- there will be no material change to macroeconomic, political, regulatory, legal or tax conditions in the markets or regions in which NortonLifeLock and Avast operate that will materially impact the implementation of, or costs to achieve, the expected cost savings;

- there will be no material divestments from the existing businesses of either NortonLifeLock or Avast;

- there will be no material change in current foreign exchange rates; and

- there will be no business disruptions that materially affect either company, including natural disasters, acts of terrorism, cyber-attacks and/or technological issues or supply chain disruptions.

Reports

As required by Rule 28.1(a) of the Code, Deloitte, as reporting accountants to NortonLifeLock, and Evercore, as financial adviser to NortonLifeLock, have provided the reports required under the City Code. Copies of those reports were set out in the Rule 2.7 Announcement.

As required by Rule 27.2(d) of the Code, the NortonLifeLock Directors confirm that:

1. there have been no material changes to the Quantified Financial Benefits Statement since 10 August 2021 and the Quantified Financial Benefits Statement remains valid; and

2. each of Deloitte and Evercore has confirmed to NortonLifeLock that their respective reports produced in connection with the Quantified Financial Benefits Statement continue to apply.

Notes

(1) The Quantified Financial Benefits Statement relates to future actions and circumstances which, by their nature, involve risks, uncertainties and contingencies. In addition, due to the scale of the Combined Company, there may be additional changes to the Combined Company's operations. As a result, the estimated synergies referred to may not be achieved, or may be achieved later or sooner than estimated, or those achieved could be materially different from those estimated.

(2) The Quantified Financial Benefits Statement should not be construed as a profit forecast or interpreted to mean that NortonLifeLock's earnings in the first full year following the date on which the Merger becomes effective, or in any subsequent period, will necessarily match or be greater than or be less than those of NortonLifeLock or Avast for the relevant preceding financial period or any other period.

(3) For the purposes of Rule 28 of the Code, the Quantified Financial Benefits Statement is the responsibility of NortonLifeLock and the NortonLifeLock Directors.